

District of Columbia Government
Department of Insurance and Securities Regulation

Anthony A. Williams
Mayor



Lawrence H. Mirel
Commissioner

MEMORANDUM

TO: John Koskinen
City Administrator

FROM: Dana Sheppard
Senior Counsel

DATED: July 15, 2002

Re: Department of Insurance and Securities Regulation's Summary of the Review Process of the Proposed Conversion and Acquisition of CareFirst

The following is a summary of the process that will be used by the District of Columbia Department of Insurance and Securities Regulation ("Department of Insurance") in its review of the proposed conversion and acquisition of CareFirst, Inc. The District of Columbia Office of the Corporation Counsel ("OCC") will also review the transaction, and has summarized their review process separately. Please contact the Office of the Corporation Counsel for information about their review process, or you may visit the OCC website at <http://occ.dc.gov>.

Group Hospitalization and Medical Services, Inc. ("GHMSI"), the District's nonprofit Blue Cross Blue Shield plan, also known as Blue Cross Blue Shield of the National Capital Area, has operated as a nonprofit health insurer in the District since 1939. In addition to providing health insurance to District residents and businesses, GHMSI also sells its products in Montgomery and Prince Georges Counties, Maryland, and in Northern Virginia, north of Route 123. In 1997 GHMSI affiliated with Blue Cross Blue Shield of Maryland, and formed a Maryland-based holding company known as CareFirst, Inc. ("CareFirst"). In 2000 CareFirst, affiliated with Blue Cross Blue Shield of Delaware. All three of the companies are currently organized and operated as nonprofit companies.

On January 11, 2002, WellPoint Health Networks Inc., a California-based for-profit health insurer ("WellPoint"), filed an application with the Department of Insurance seeking permission to convert GHMSI to a for-profit company, and acquire its assets. WellPoint also filed similar applications in Maryland and Delaware to convert and acquire their nonprofit Blue Cross Blue Shield Plans. WellPoint has offered the three jurisdictions a total of \$1.3 billion for the entire CareFirst entity.

WellPoint's applications must be approved by the Insurance Commissioners in each of the three jurisdictions before the conversion and acquisition of CareFirst can occur. In addition, the District's Corporation Counsel, and the Attorneys General of Maryland and Delaware must review and approve the application before the conversion and acquisition can occur. In other words, WellPoint will not be permitted to acquire CareFirst and its subsidiaries unless it receives prior approval from the District, Maryland and Delaware. Accordingly, if any of the three jurisdictions disapprove the transaction, neither the conversion nor the acquisition will take place. In addition, Congress will also have to enact legislation to permit the conversion and acquisition of GHMSI because GHMSI's charter was granted by an act of Congress.

In general terms, the role of the Insurance Commissioner of the Department of Insurance is to ensure that the proposed conversion of GHMSI from a nonprofit to a for-profit company is in the public's interest, that the resulting for-profit company would be a financially viable entity, and that GHMSI's policyholders and the insurance-buying public will not be harmed as a result of the conversion and acquisition. WellPoint must satisfy the provisions of the Holding Company Act (D.C. Official Code § 31-703), and the Hospital and Medical Services Corporation Regulatory Act (D.C. Official Code § 31-3515).

The Department of Insurance made a preliminary determination that the WellPoint application failed to include information necessary for the Department of Insurance to undertake a proper review of the proposed transaction. Accordingly, the Department of Insurance has asked WellPoint to file an amended application no later than August 12, 2002. The Department of Insurance will continue its review of the WellPoint's application when it is resubmitted. The Department of Insurance will hire outside experts from various disciplines to assist it in the review of the proposed transaction.

The Department of Insurance has hired the law firm of Mitchell, Williams, Selig, Gates & Woodyard, a firm with substantial insurance regulatory experience, to assist in the review of the transaction. In addition, the Department of Insurance plans to hire a financial expert that has insurance and actuarial expertise to examine the financial aspects of the transaction. The Department of Insurance will also hire a firm to review GHMSI's role of providing health insurance in the District of Columbia, and the impact on the health insurance market in the District if GHMSI is permitted to become a for-profit health insurer.

The Department of Insurance will examine the specifics of the proposed transaction as it relates to the District and neighboring jurisdictions, as well as WellPoint's acquisitions in California, Missouri, and Georgia to determine what effect, if any, the proposed transaction will have on the products, services, and rates currently being offered to individuals, small groups, large groups, and those in the federal employee program. Our insurance and actuarial experts will examine the proposed transaction and advise us about the potential for any increases in the number of uninsured persons in the District, including whether WellPoint would have to increase health insurance premiums or reduce services as a result of the acquisition. The Department of Insurance will also examine the proposed transaction to determine what impact, if any, it will have on healthcare providers.

The financial and health insurance experts will prepare a written report that will be included in the public record, and made available to the public. We anticipate that these experts will require a minimum of three months to complete their reviews. The Department of Insurance will select all of its experts, but all of the fees and expenses of those experts will be paid by WellPoint directly to the experts. No District funds will be spent on experts.

The Office of the Corporation Counsel will have the primary responsibility of determining whether the price being offered for GHMSI is adequate and, if the transaction is approved, to ensure that any funds received will be used to further GHMSI's original charitable mission. The Department of Insurance will work with the Office of the Corporation Counsel during this part of the review process.

The Department of Insurance will permit organizations and persons seeking "party" status to file motions to intervene beginning on July 16, 2002. The last day to file motions to intervene will be August 16, 2002. A person or organization granted "party" status will be permitted to conduct discovery prior to the evidentiary hearing that is tentatively scheduled to be held December 2 through 5, 2002. In addition, "parties" will be allowed to present direct evidence and cross-examine witnesses at the hearing. In addition to the right to participate, "parties" will be required to respond to discovery requests, attend status conferences, and submit to cross-examination at the hearing. The Department of Insurance will publish proposed hearing procedures during the month of July, which will be final prior to the beginning of the public hearing. These procedures will contain additional information about the hearing process and the rights and responsibilities of participants. Additionally, the Department of Insurance will publish notices of the public hearing in the *Washington Post* at least 30 days prior to the public hearing.

Those organizations and persons that do not want to participate as "parties" will be given the right to make an oral presentation at the hearing or submit written testimony, which will be included in the public record. Such persons will not be allowed to conduct discovery, present direct evidence, or cross-examine witnesses at the hearing. The deadline to notify the Department of Insurance of the intent to make an oral presentation at the public hearing will be November 22, 2002. The deadline to submit written statements to the Department of Insurance will be November 7, 2002.

The Department of Insurance's public hearing will proceed in many ways like a regular trial, but will be less formal. The Insurance Commissioner will be the presiding official at the Department of Insurance's public hearing, and will have the authority to determine the scope and conduct of the proceedings.

The Corporation Counsel has the primary legal responsibility to determine if the amount of money offered for GHMSI's assets is adequate. The Corporation Counsel must also ensure that any monies received from WellPoint are used for appropriate charitable purposes. Persons interested in taking a position on the "valuation" issue in the proceedings to be held by the Corporation Counsel should consult that office to determine their rights to participate regarding this issue.

The Department of Insurance plans to call the District's investment banker as one of its expert witnesses because the Insurance Commissioner must also determine if the price being offered for GHMSI's assets is adequate and appropriately used. Accordingly, anyone wanting to address the "valuation" issue in the public hearing to be held by the Department of Insurance may be allowed to participate as either a formal "party", or on a limited basis by filing a written statement, or making an oral statement at the public hearing , as mentioned above.

Representatives from CareFirst and WellPoint will present testimonial and documentary evidence in support of the proposed conversion and acquisition, which will include their plan to operate GHMSI as a for-profit entity. WellPoint and CareFirst will, among other things, attempt to establish that the proposed transaction is in the public's interest, will not adversely effect the District's health insurance market, and will not negatively impact GHMSI's financial condition. "Parties" and members of the Department of Insurance will be given the opportunity to cross-examine CareFirst and WellPoint officials and their expert witnesses on issues raised during their testimony.

After CareFirst and WellPoint have presented all of their evidence, "parties" will be given the opportunity to present testimonial and documentary evidence in support of their positions on the proposed conversion and acquisition. CareFirst, WellPoint and members of the Department of Insurance will have the opportunity to cross-examine "parties" and their witnesses on issues raised during their testimony.

Finally, the Department of Insurance and its health care and financial experts will be asked to present testimony regarding their findings. Representatives from CareFirst, WellPoint, and "parties" will be given the opportunity to cross-examine the Department's experts on issues raised during their testimony.

After the conclusion of the evidentiary hearing, the Commissioner of Insurance will issue a decision and order approving or disapproving the WellPoint application. As stated previously, the Commissioner of Insurance cannot approve the application unless the Corporation Counsel also approves the application. However, either the Commissioner of Insurance or the Corporation Counsel may disapprove the application.

For additional information, please visit our website at www.disr.washingtondc.gov or call Mr. Dana Sheppard, Senior Counsel, at (202) 442-7753.

cc: Raymond Santora
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